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# **Reflections from Comparative Studies of the Development Models in Latin America and East Asia**

**Jiang Shixue**

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# **Reflections from Comparative Studies of the Development Models in Latin America and East Asia<sup>\*</sup>**

*Jiang Shixue<sup>\*\*</sup>*

Since the early 1980s, the international academic circles have shown keen interest in comparing the economic development models in Latin America and East Asia. Their interest in the two regions is easy to comprehend. In the middle of the 20<sup>th</sup> century Latin America was at a higher level of development than East Asia. However, in the thirty years from 1960 to 1990, the fastest-growing economies are concentrated in East Asia, and the slowest in Africa and Latin America. In the Republic of Korea, the world's fastest growing economy between 1960 and 1990, per capita GDP grew at an average of 6.7 percent a year, rising 700 percent in thirty years (see table 1). Several Asian economies rose many steps on the per capita income ladder between 1960 and 1990. South Korea rose forty-six steps, Thailand thirty, and Singapore twenty-six. In contrast, many Latin American countries, including Argentina and Venezuela, dropped many steps on the ladder, fourteen for Argentina and twenty for Venezuela (Alesina, 1997: 218).

This paper will not repeat what have been commonly acknowledged as the basic causes explaining the different economic performance between Latin America and East Asia. Rather, it will try to present some reflections from the comparative studies of the development models in the two regions.

## **1. Development theories need to develop.**

With the political independence of many developing countries in the middle of the 20<sup>th</sup> century, development economics came into being. Economists with various ideological orientations put forward many theories regarding the possibility and ways of development in the developing

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world. Undoubtedly, some theories were helpful in guiding decision-makers when they dealt with all sorts of economic problems. However, there are theories that have become quite misleading or even dated.

The first such theory that comes into our mind is the *dependencia* (dependence theory), which was quite prevalent in much of the Third World in the 1960s and 1970s. There are distinct versions of *dependencia* ranging from the analytic assessment of scholars such as Theodore Moran to the more overtly political and ideological writings of Andre Gunder Frank and Fernando Henrique Cardoso (Wiarda, 1999:75). According to this theory, one of the causes of underdevelopment in the developing world is its dependence upon the industrial countries in such areas as market, capital and technology. Therefore, for the Third World to develop, the only way is to “de-link” with the developed countries and the world economy.

It is right for the *dependencia* to point out the nature of the unequal exchanges between the North and the South. However, it should be pointed out that it neglected the benefits of integrating a given national economy with the world market. Particularly, with deepening interdependence in the age of globalization, it is highly necessary for the developing countries to choose an outward-oriented path of development.

It is interesting to note that even A. G. Frank once acknowledged that “de-link” was difficult or even impossible for the developing countries.<sup>1</sup> Indeed, in today’s world, de-link will end up in marginalisation.

## **2. Economic growth should be accompanied by equal income distribution so that economic benefits can be shared justly by everyone in the society.**

East Asia has been doing better than Latin America not only in terms of economic growth but also in the areas of social development. Economic reforms of the early 1990s in Latin America did reduce poverty by a few percentage points, but population growth made the absolute number soared. The region’s gap in the UNDP’s *Human Development Index* has been reduced

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<sup>1</sup> Florida International University: *LACC News* Autumn, 1993.

by more than 20 percent between 1975 and 1997, reflecting a substantial improvement in social indicators. However, poverty remains stubbornly high, affecting 36 percent of the Latin American population, or some 185 million people, (Aninat, 2000:2).

The poverty issue in Latin America is related to many causes, and unequal income distribution must be one of them. Indeed, Latin America shows startling contrasts, between the rich and poor, between city and countryside, between the powerful lord of the hacienda and the deferential peasant, between wealthy entrepreneurs and desperate street urchins (Skidmore, 1997:3). As table 1 indicates, Latin America is among the world's several regions where income distribution is the worst.

Latin American policy-makers seemed to have been influenced by the following reasoning in dealing with the relationship between growth and income distribution: One was the belief that the benefits from economic growth would automatically “trickle down” to the poor people, and market forces would do the job of distributing income equally. Another assumption came from the belief that the government would be concerned with the fate of the poor and would make proper policies to improve their income. Finally, it was hoped that, in the early stage of development, the poor had to undergo a process of “belt tightening”, and the rich tended to use their wealth to invest more in the economy, thus benefiting the poor as well.

Apparently, the above three justifications turned out to be totally wrong. The “trickle down” did not happen and the market force itself would not redistribute income for the benefits of the poor. From time to time the government, whether democratic or authoritarian, made policies that worsened income distribution. And, the rich did not increase their investment out of their increasing wealth. They consumed more instead. It was found that small farmers saved at least as high a proportion of their income as big landlords (Streeten, 1979).

Unequal income distribution is not only an economic issue, but also a political one. It has caused much political and social unrest in Latin America. The most notable example is the bloody fight between the landless and the big landlords over land ownership in many countries,

particularly in Brazil in recent years. One of the causes for the Chiapas uprising is poverty, which had been worsened by unequal income distribution.

The experiences of East Asia's development show that education can help improve income distribution. Education not only benefits personal career directly, but also improves overall economic prospects for the nation. Progress made in education has been impressive in Latin America. Quite a few countries in the region now have universal primary education, and enrolment in both secondary and university education has rapidly increased (Urrutia, 1991:40). However, compared with some of the other developing countries, particularly those in East Asia, Latin American country's progress in education has been limited.

Table 1     Income Distribution in Latin America and East Asia  
(Gini coefficient)

	1960s	1970s	1980s
Latin America			
Brazil	0·53	0·60	0·57
Chile	0·46	0·46	...
Mexico	0·55	0·50	...
Colombia	...	0·57	...
Costa Rica	0·50	0·49	0·42
Average	0·51	0·52	0·50

East Asia			
Korea	0.34	0.39	0.36
Singapore	...	0.37	0.42
Hongkong	0.49	0.43	0.45
Thailand	0.41	0.45	0.47
Malaysia	0.42	0.53	0.48
Indonesia	0.33	0.32	0.31
Average	0.38	0.40	0.39

Source: Nancy Birdsall and Frederick Jaspersen (eds.): *“Pathways to Growth: Comparing East Asia and Latin America”*, Inter-American Development Bank, 1997, p.87.

### **3. The relationship between government and market needs to be dealt with properly.**

In recent years the relationship between government and market has been one of the hottest debated issues in the field of economics and political sciences.

Lawrence Summers summarizes this relationship under four interrelated broad headings: human and physical infrastructure, competitive climate for enterprise, macroeconomic management and institutional development (Summers, 1993:244). Others might add more provocative thoughts. In any case the central question is how to integrate theory with reality.

In the 1950s, ECLAC assigned the state a very important role in the pursuit of the ISI model such as designing and carrying out an industrial program, and protecting the domestic market against foreign competition. Indeed, as Enrique V. Iglesias, the IDB President and a native of Uruguay, once said, “Our generation was one that believed strongly in the role of the state.”<sup>2</sup>

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<sup>2</sup> E. Iglesias, “From Policy Consensus to Renewed Economic Growth”, in John Williamson (ed.): *Latin American Adjustment: How Much Has It Happened?* Institute of International Economics, Washington, DC, 1994, pp. 345-346.



Although ECLAC suggested strongly that the state should play an important role in the economy, it also warned of the danger of excessive intervention. But ECLAC's call, particularly the new ideas of neo-structuralism or "updated structuralism" regarding the relationship between the state and markets, often fell on deaf ears.

Starting from the late 1980s neo-liberalism or Washington Consensus began to sweep across the whole continent of Latin America. According to this doctrine, government should greatly reduce intervention in the economy by abolishing regulations that impede the entry of new firms or restrict competition, and ensuring that all regulations are justified by such criteria as safety, environmental protection, or prudential supervision of financial institutions.<sup>3</sup>

In pursuing the model of openness and deregulation, Latin American countries have privatized many SOEs. Indeed, privatization has marked a new chapter in Latin America's program of structural reforms, reversing decades of state intervention. According to the Inter-American Development Bank, Latin America has been a leader in the developing countries' efforts to privatize. The \$59 billion that Latin America realised from its 694 divestitures over the 1990-1994 period is more than half the \$104 billion realised by all developing countries. It far exceeds the \$20 billion realised by East Asia and the \$15 billion obtained by Europe and Central Asia (IDB, 1996:169).

However, it seems that too much faith was placed in the capacity of privatization and market. Experience from implementing the ISI model and the model of openness and deregulation signifies that success at managing the economy will require not a zero government role but instead a modified one, although this role has to involve a decrease in government's public responsibilities. Particularly in those countries with the experience of much liberalisation,

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<sup>3</sup> In addition to privatization and deregulation, the Washington Consensus also suggests the following: fiscal discipline, public expenditure priorities, tax reform, financial liberalization, competitive exchange rates, trade liberalization, and abolishing barriers impeding the entry of foreign capital. See John Williamson (ed.): *The Political Economy of Policy Reform*, Institute of International Economics, Washington, DC, 1994, pp. 26-28.

whether in the financial sector or in other areas, government regulation/supervision is all the more important. The peso crisis of Mexico in 1994 was a proven example in this regard.

In the new century, with conditions of development changed significantly both internally and externally, the state in Latin America will be required to re-establish itself as an effective manager and supervisor for the liberalised economy. But this new role should be very different from that of the past. As Naim puts it, the more difficult task for the Latin American governments would be the reintroduction of the state, but not as the incompetent, corrupt owner-manager of airlines and steel mills, not as the myopic picker or subsidised “priority” industries that made inferior products at inflated prices, and not as the administrator of a constantly mounting pile of absurd economic regulations that boosted corruption and depressed growth. Rather, the “new” state should rebuild its capacity and ability to provide basic public goods and services, to collect taxes, to regulate effectively and honestly the activities of the private sector, to support local firms in international expansion, and to ensure that economic benefits can be spread to everyone in the society (Naim, 1993:27).

Indeed, in the words of Michel Camdessus, it is necessary to establish an arms-length relationship between governments and markets, neither too close nor too distant.<sup>4</sup> For Latin American, East Asian and other developing countries, the challenge is how to determine this “arms-length” under the new development model.

#### **4. International competitiveness matters.**

It is interesting to note that Paul Krugman argues in the March-April 1994 issue of *Foreign Affairs* that competitiveness is a meaningless word when applied to national economies, and the obsession with competitiveness is both wrong and dangerous. He says, “The idea that a country’s economic fortunes are largely determined by its success on world markets is a hypothesis, not a necessary truth; and as a practical, empirical matter, that hypothesis is flatly

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<sup>4</sup> Michel Camdessus: “Governments and Economic Development in a Globalized World”, Remarks at the 32<sup>nd</sup> International General Meeting of the Pacific Basin Economic Council, Hong Kong, May 17, 1999.

wrong...Thinking in terms of competitiveness leads, directly and indirectly, to bad economic policies on a wide range issues, domestic and foreign, whether it be in health care or trade.” The well-known American economist goes on to write: “So when we say that a corporation is uncompetitive, we mean that its market position is unsustainable – that unless it improves its performance, it will cease to exist. Countries, on the other hand, do not go out of business. They may be happy or unhappy with their economic performance, but they have no well-defined bottom line. As a result, the concept of national competitiveness is elusive.”(Krugman, 1994)

Krugman’s argument might be misleading. It is not suitable for him to compare a nation’s economy to the business performance of a company. As a matter of fact, in the age of globalisation, competition tends to become fiercer than ever in the world market. So it is highly necessary to strengthen competitiveness. For any country, particularly a developing one, if there is no competitiveness, there will be no chance to gain overseas market share

Generally speaking, the extent and degree of competitiveness is closely related to exports. For Latin America, exports were at the centre of the model of exporting primary commodities. The ISI model neglected export promotion. In the 1950s, Latin America accounted for 12.5% of world exports. In 1990, this percentage declined to less than 3.5%, the lowest point in a century (Naim, 1995:57).

The model of openness and deregulation has attached great importance to exports as the “engine of growth”. This approach has worked rather successfully. Between 1987 and 1994, regional exports grew at around 10 percent per annum in real dollar terms and 6 percent in volume (Burki, 1996:12). No less important has been the fact that the region seems to have diversified its export structures.

Globalisation brings both opportunities and challenges. On the one hand, Latin America and any other country in the world will face a larger world market; on the other, every country will try to gain a bigger market share. Therefore, in order to expand exports on a solid base, Latin

America should increase its competitiveness through productivity improvements.<sup>5</sup> To meet this end, first of all, the region needs to take advantage of the rapid development of the so-called “technological revolution” and “information revolution” to upgrade its industrial structures.<sup>6</sup> The objective of this task, *transformacion productiva* in ECLAC’s words, is to make economic activities move in the direction with a higher value added and a higher growth potential. In addition, reliance upon traditional exports of primary products needs to be reduced and non-traditional exports, especially manufactured exports, should be encouraged.

### **5. Agricultural development should not be neglected in the process of industrialization.**

In many parts of the Third World, there are examples of agricultural progress. In some cases, agricultural organization, particularly in export agriculture, is even quite modern. For the most part, however, agricultural retardation has been evident in many parts of Latin America. In consequence, agricultural productivity has lagged behind industrial productivity in many Latin American countries.

During the 1960s and 1970s, while the economy grew at rates above the world average, the agricultural sector, constrained by the ISI model that prioritised the manufacturing sector, developed at rates somewhat below the world average (Reca, 1997).

Compared with East Asia, Latin America’s agricultural sector had been discriminated and neglected in the following aspects:

First, the government allocated more resources to the manufacturing sector at the expense of less agricultural investment. At the same time, the government also used exchange rate policies and protection to favor the manufacturing sector. Needless to say, when one sector was favored,

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<sup>5</sup> However, as Samir Amin points out in a lecture presented at the Chinese Academy of Social Sciences in September 2000, competitiveness should be gained at the expense of lowering wages for the worker.

<sup>6</sup> As an ECLAC document points out, however, it is worth noting that the most important impact of the current technological cycle on employment is the obsolescence of certain skills and know-how. Consequently, some jobs are eliminated and others are created (See ECLAC: *Latin America and the Caribbean: Policies to Improve Linkages with the Global Economy*, 1999).

another would be in a disadvantageous position.

Second, although governments of Latin America have kept on talking about reforms of the agricultural sector, sometimes even including land redistribution, the reality was that, other than the Mexican and Bolivian reforms, results and effects have been quite disappointing (Glade, 1991:148). So the numbers of landless have been growing, and the problem of rural poverty is yet to be resolved.

Third, although price control was considered an instrument of social policy, it has in fact reflected the political power of the urban interests and has created huge losses for the rural residents. In addition to discouraging production and leading increased food imports, price control had pushed the farmers out of the fields to live in the urban areas, thus worsening the unemployment issue in many countries (Balassa, 1986:92).

Agricultural retardation in Latin America has had two negative results. On the one hand, since agricultural growth in many countries has failed to keep up with population growth, governments have to allocate scarce foreign exchanges to import food. On the other, rural income cannot be raised and the gap between the urban and the rural has grown all the time.

## **6. In the age of globalization it is still important to strike at a correct balance between opening to the outside world and protecting domestic market.**

For decades, due to the ISI (Import Substitution Industrialization) model, the governments of Latin American countries built high walls of protection for the domestic market, resulting in a range of tariffs and procedures to control imports. Effective rates of protection of one thousand percent or even more were not uncommon (Hojman, 1994:205). The “lost decade” of 1980s worsened these practices.

The picture has changed completely since the late 1980s. If in the days of the ISI model, isolation was the rule in Latin America, now openness is the order of the day. Trade liberalization introduces foreign competition, forcing the domestic enterprises to raise efficiency. At the same time, however, many local firms were hard to face the sudden increase

of challenges and went bankrupt, worsening the unemployment problem.

Despite the harsh reality, it is not wise to shut the door again and keep out foreign competition. But, opening the door does not mean that trade liberalization should be realised overnight and no protection could be applied. The Latin American experience seems to make the following two points more conspicuous:

First of all, speed of opening the domestic market is important. Whereas Brazil and Venezuela liberalised their tariff regime over a few years, Mexico, Argentina, Colombia and Peru conducted faster trade liberalization (Loayza, 1997:4). It seems that a gradual approach is more ideal in trade liberalization, simply because the local enterprises need time to adjust to the changes of market conditions.

Second, following the globalization trend does not mean that there should be no protection and safeguard for the domestic market. Introducing foreign competition can force domestic enterprises to be aware of the necessity of raising efficiency. But this should be carried out in a gradual way. Sudden opening without proper protection will result in an awkward situation for the local firms. In this regard, “dancing with the wolf” is certainly dangerous.

## **7. Domestic savings rates should be raised to promote capital accumulation and reduce dependence upon foreign capital.**

Both in theory and in reality, capital accumulation plays an important role in economic development. As a World Bank report notes, countries that grow faster devote a higher proportion of their GDP to investment and have developed a capital market that helps channel these funds towards high return projects. A faster rate of capital accumulation requires an increase in domestic savings (Burki, 1996:14).

Latin America is well known for its low saving rates. In 1980 the region saved on average 19 percent of its GDP; by 1994 this ratio was basically unchanged. To maintain growth momentum, Latin America has been relying heavily on foreign capital, including foreign direct investment,

portfolio investment and bank loans.

Foreign capital has made great contribution to Latin America's economic development. However, it has its side effects, risk and challenges. According to a World Bank research, at the macro level, large foreign capital inflow can affect an economy's competitiveness, saving, and investment performance, expose it to external shocks, and ultimately reduce its degree of policy independence from the rest of the world. At the micro level, sustained capital inflows can have profound effects on the policies of the financial, industrial, and other sectors, on the shape and regulation of domestic capital markets, and even on the extent and form of government activities in the economy. Furthermore, since not all external capital flows have the same nature and features, different types of such capital will have the different effects on the host economy (World Bank, 1996:1-2).

As a matter of fact, Latin America has bitter experience in this regard. As mentioned earlier, the region was hit by a foreign debt crisis. Then came the Mexican peso crisis in 1994. With the quick outflow of foreign funds, mainly "hot money" of speculative nature, the tequila effect spread to other Latin American countries and even to some other parts of the world.

In a word, foreign capital is not a long-term reliable source of funds, or a substitute for domestic savings as a means for financing investment. The best possible way to reduce dependence upon foreign capital is to raise domestic savings rates.

For Latin America, how to raise savings rates is certainly not a difficult task. It seems that leaders of the region should pay attention to such policy actions as improving income distribution, establishing more efficient financial institutions to mobilise savings and changing the consumption habits of the rich, among others.

## **8. Political stability should go hand in hand with economic development.**

The relationship between politics and economics is always controversial. While some say that political democracy is the prerequisite for rapid economic growth, others argue that economic development needs political authority that might limit democracy. A number of studies have

found that there is no systematic relationship between democracy and rates of economic growth. It is hard to turn a blind eye to the fact that most of the major economic success stories – for example, Chile, South Korea or Singapore – had governments that were authoritarian in many respects (Summers, 1993:251).

Implementation of each of the development models in Latin America and East Asia was not purely an economic matter. In other words, effectiveness of any model is conditioned by some non-economic factors, and political development was one of the most important.

It is true that some countries in Latin America and East Asia, such as Brazil and Chile, made remarkable economic achievements during their military rule, the so-called bureaucratic authoritarianism. Nevertheless, some other Third World countries where no progress of political democracy had been established failed to develop the economy. Therefore, it seems that political democracy is not the sole condition for economic growth.

As a matter of fact, the essence of the relationship between economic and political development points to the necessity of maintaining political and social stability, a condition highly necessary for rapid economic development. Also, political development is often related to government credibility, which, once lost, is restored only very slowly. As a result would-be foreign or domestic investors would always delay investment, waiting to see how things turn out before deciding whether to invest. Experience has shown that, to make radical economic reforms in Latin America, you need to have a high degree of political consensus. If a democracy is to manage what in the words of Aylwin, the former president of Chile, amounts to an “economic coup”, the quality of politics must be very high.<sup>7</sup>

In conclusion, a study of the development models in Latin America and East Asia reveals:

- 1) development theories need to develop in the age of globalization;
- 2) economic growth should be accompanied by equal income distribution so that economic benefits can be shared justly by everyone in the society;

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<sup>7</sup> *New Perspective Quarterly*, Fall 1993, p. 18.



- 3) the relationship between government and market needs to be dealt with properly;
- 4) international competitiveness matters;
- 5) agricultural development should not be neglected in the process of industrialization;
- 6) in the age of globalization it is still important to strike at a correct balance between opening to the outside world and protecting domestic market;
- 7) domestic savings rates should be raised to promote capital accumulation and reduce dependence upon foreign capital;
- 8) political stability should go hand in hand with economic development.

### **9. Economic policies are more important than cultural factors in determining economic performance.**

Cultural factors have been used to explain the Asian economic “miracle” and the Asian crises. As a matter of fact, there is not just one explanation for the differing economic performance in East Asia and Latin America. However, we should not throw away with the bath water of cultural determinism all the healthy babies of hypotheses about the following points:

First, the cultural approach has opened a door for us to see why economic performance is different among regions and countries. As Alvin Y. So and Stephen W. K. Chiu point out, the cultural approach is not aimed at reducing economic development to a set of cultural traits or “national character” traits. The key question is not whether the cultural factor is the exclusive influence over economic performance; rather, it relates development policy options and institutional choices to certain cultural antecedents that make the reason for such selections easier to be understood.<sup>8</sup> In other words, cultural perspective provides researchers with a frame of reference within which they can see how values, attitudes, practices or behaviours have influenced economic development in East Asia and Latin America. Therefore, it complements rather than contradicts other interpretation of the so-called East Asian “success” and Latin American “failure”.

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<sup>8</sup> See Alvin Y. So and Stephen W. K. Chiu: *East Asia and the World Economy*, Sage Publications, 1995, p. 8.

Second, although culture plays an important role in economic performance, as it can affect people's behaviours and attitudes towards savings, education, work ethic and so on, yet compared with economic factor, it is less important. Of all the factors determining economic performance, economic factor always stands on top.

Third, each culture has its own unique positive or negative components, but the positive ones cannot automatically create better economic performance in the absence of other necessary conditions like sound economic policies, effective institutions, favourable world economic situations, the right timing of a nation's entry into industrialisation, and political stability. In other words, only in a favourable economic and political environment can culture trigger economic growth. This point might help explain why China, the birthplace of Confucianism, can make remarkable economic achievements during the past two decades of economic reforms.

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